Statenews: The Council of State Governments

"Paving the Way"

By Mikel Chavers

In 2002, Virginia was in a tight spot.
The state had been through a decade of traditional planning for the Capital Beltway and the price tag for the project was colossal at nearly $3 billion.
"It was unaffordable and unachievable," said Pierce Homer, Virginia's secretary of transportation.
Then the private sector came forward with an idea for the road. The company wanted to do something more innovative. It wanted to do something different.
And what Virginia's department of transportation found in the private sector's idea is the central appeal of the concept of public-private partnerships in transportation today. The idea, in private industry's hands, solved 85 percent of the problems for about a third of the cost, Homer said. So the state made a partnership.
"They had built a better mouse trap," Homer said.

Widespread Trend

When it comes to funding transportation projects, the Federal Highway Administration reports 22 states and one U.S. territory have passed legislation that allows for deals between public entities and private enterprise to finance road projects.
While the partnerships take on various forms, many of them are toll roads.
"Practically every state in the country is contemplating tolls," said Sujit CanagaRetna, senior fiscal analyst for The Council of State Governments' (CSG) southern region, the Southern Legislative Conference.
"It's increasingly becoming apparent that states can't rely on the federal government, mainly through the Highway Trust Fund," he said.
The Highway Trust Fund, the federal pot of money used to fund road projects, is drying up. Spending in 2007 and 2008 will exceed money coming into the account and the fund will go bust by a projected $4 billion, according to July 2007 estimates from the Office of Management and Budget.
Another option is to raise state gas taxes to meet the transportation budgeting shortfall, but "raising taxes in this political environment is very toxic," Canaga-Retna said.
So states are turning to the private sector—and there's money to be had.
The Federal Highway Administration estimates hundreds of billions of dollars in private equity is available worldwide, "just waiting on the sidelines," said Jim Ray, the Federal Highway Administration's acting deputy administrator.
With that in mind, states like Virginia are getting creative as public-private partnerships can take on various forms, experts say.
"Public-private partnerships start as a blank sheet of paper," Ray said. "The only limitation of what we can harness of the private sector is our own willingness to be creative."

States Get Creative

Although the idea of a pubic-private partnership is nothing new, certain aspects are making these projects new and novel ideas, CanagaRetna said.
"What is interesting is states are now finally creating legislation that allows for these partnerships to gel," he said.
Twelve years ago Virginia enacted the Public-Private Partnership Act of 1995 and since, the state has several public-private projects under its belt.
The Dulles Greenway, dedicated in 1995, was the state's first private toll road in more than 100 years.
There's also the Capital Beltway, the road bordering Washington, D.C., that is one of the most congested roads in the country. With that project, Virginia is partnering with construction firms Fluor Enterprises and Transurban to build high occupancy toll lanes on a 14-mile stretch of Interstate 495 beginning in 2008. While carpoolers and buses won't be charged to drive the special lanes, vehicles with just one person will pay a toll, which will be based on congestion pricing.
In congestion pricing, the price of a toll changes based on the time of day. At peak times the toll is more expensive, while at slower times, the toll is cheaper. Homer said this innovative pricing model will help control congestion

on the road and is what makes the idea fitting for private sector involvement.

"What (the private sector is) betting on is how people value their time. They're willing to take the entrepreneurial plunge and take that risk," Homer said.

North Carolina is also interested in using new technology when it comes to tolls, said Grady Rankin, chief fnancial officer for the North Carolina Turnpike Authority. Although his organization has not constructed any roads yet, the group is looking into using cashless systems to collect the proposed tolls.

Cashless methods can use video monitoring to capture license plates on vehicles as they drive through the toll area in order to bill a driver for payment. Other cashless systems use radio frequency identification tags on vehicles, which are scanned as they pass through the toll road's checkpoint.

For the proposed Triangle Expressway project in the Raleigh, N.C., area, officials are considering all-electronic methods to collect tolls. The turnpike authority's consultant team reported in September that electronic methods of tolling could save 7 percent of the project's total cost, estimated at $850 million. That could mean $60 million in savings just by implementing electronic tolling on the expressway, according to the consultants' report.

Partnerships Take on Risks

Part of determining the creative approach to a public-private partnership, Homer said, is defining where there are clear risks and benefits suitable for the private and public sectors. A good public-private partnership, he said, is when there is "sufficient risk put off of the public sector."

But that doesn't mean there are no risks for the state. Worst-case scenario, he said, would be if a partnership project does not succeed and doesn't garner enough revenue. But that's where performance or escape clauses in the contracts are important, Homer said.

That risk, however, is something states have seen firsthand in recent years. In Virginia, for example, when traffic on the Dulles Greenway fell short of what was originally predicted, it caused financial strain. So in 2005, an Australian company purchased a portion of the toll road for $533 million.

The potential for traffic estimates to be wrong is one valuable lesson learned so far, said Ray of the Federal Highway Administration.

"The traffic modeling is a little more of an art than it is a science, especially when you start looking 20 or 30 years out," Ray said.

And with long-term lease deals becoming a part of public-private partnerships, some critics are wondering if looking that far ahead is a smart decision for states to make.

In Texas, the state awarded a 50-year contract to a Spanish company to operate State Highway 121 as a toll road. Cintra will provide more than $5 billion—$2.1 billion up front—for the road and other projects in north Texas, according to the Texas Department of Transportation Web site. The agreement will have the road completed by 2011, a quarter century faster than would have been possible with traditional gas tax revenue, the site reports.

Other long-term leases of roads to private companies include the Chicago Skyway, leased for 99 years to a consortium jointly owned by Australian company Macquarie Infrastructure Group (MIG) and Spain's Cintra. Under the lease, the consortium will operate and maintain the tollway for nearly a century.

Indiana also inked a 75-year lease in June 2006 with Statewide Mobility Partners for the operation and maintenance of the Indiana toll road.

Some States Face Opposition

But some states are finding significant opposition to proposed public-private partnerships, which in some cases, could even jeopardize hundreds of millions of dollars in federal funds.

In Texas, the use of private equity in road projects, including the proposed massive Trans-Texas corridor system, recently came under criticism. State lawmakers called for a two-year moratorium on toll road projects being built by private companies that have contracts with the state's transportation department. While the bill won't stop a few listed highways from being built as public-private partnerships, it will prevent most public-private projects from moving forward for the time being.

"Hopefully, by the time we go back in 2009, we will have identified shortfalls in infrastructure needs and identified different funding mechanisms to decide how to pay for the needs that have been identified," said Texas Rep. Lois Kolkhorst, who serves the state's District 13.

Kolkhorst was the author of amendments on the bill, Senate Bill 792, which placed the temporary hold on the state's publicprivate partnerships.

"We went from two projects to multiple," she said. "We were starting to introduce this concept in areas of highways that were never conceived to be used for private equity."

At one point, more than 20 projects were being considered as public-private partnerships, she added.

And in Pennsylvania, after plans to toll Interstate 80 circulated, two U.S. representatives from Pennsylvania sponsored an amendment to an appropriations bill that would bar federal funds from being used to toll I-80 or improve the state's portion of it. That bill, the Transportation, Housing and Urban Development Appropriations fiscal year 2008 bill (H.R. 3074), still includes a similar amendment.

"I think the learning curve of using private equity is very steep," Kolkhorst said.

"P3 projects should not drive a transportation program. Public-private partnerships are a tool to achieve the overall goal of a transportation program," Homer, from Virginia, said.

Criticism Highlights Key Issues

The U.S House Transportation and Infrastructure Committee criticized the use of public-private partnerships that "are not in the long-term public interest." That's according to a May 10 letter from the committee's chairman, Minnesota Rep. James Oberstar and Oregon Rep. Peter DeFazio, chairman of the Subcommittee on Highways and Transit.

The letter expressed concern over the "rush of the Administration and some states to embrace PPPs," warning that the committee will "work to undo" any of these public-private partnerships.

Texas Gov. Rick Perry responded to Oberstar and DeFazio's letter with his own in July, saying, "I would hope that the federal government would encourage innovation and not stifle it."

Oberstar and DeFazio followed up their May later with a June paper that elaborated on criticisms of public-private partnerships, highlighting noncompete clauses sometimes included in the agreements. The June paper said the noncompete clauses limit the ability for state and local governments to "meet current and future mobility and safety standards for the traveling public."

The Indiana Toll Road's 75-year deal included a noncompete clause that prohibits the state from building or improving limited access highways within a 10-mile corridor on either side of the toll road.

Kolkhorst from Texas said even though some of the Texas public-private partnership contracts didn't include stated noncompete clauses, stipulations in the contracts worked in much the same way. Those contract terms led to the legislature's uneasiness and eventually to the two-year pause on the majority of the public-private deals, she said.

But the criticisms haven't swayed the Federal Highway Administration's support of public-private partnerships.

"We haven't changed one bit," Ray, the acting deputy administrator, said. "We think that state leaders are responsible individuals and that they have the public's interest at heart. They are closer to the public whose interests they are protecting."

—Mikel Chavers is associate editor of State News magazine.

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